

Notice of Proposed Regulatory Action

The State Board of Equalization Proposes to Adopt Amendments to California Code of Regulations, Title 18, Section 1685.5, *Calculation of Estimated Use Tax - Use Tax Table*

NOTICE IS HEREBY GIVEN

The State Board of Equalization (Board), pursuant to the authority vested in it by Revenue and Taxation Code (RTC) section 7051, proposes to adopt amendments to California Code of Regulations, title 18, section (Regulation) 1685.5, *Calculation of Estimated Use Tax - Use Tax Table*. Regulation 1685.5 prescribes the manner in which the Board “shall annually calculate the estimated amount of use tax due according to a person's adjusted gross income and by July 30 of each calendar year make available to [the] Franchise Tax Board such amounts in the form of a use tax table,” as required by RTC section 6452.1, as amended by section 1 of Senate Bill No. (SB) 86 (Stats. 2011, ch. 14). The proposed amendments update the manner in which the Board shall annually calculate the estimated amount of use tax due according to a person's adjusted gross income (AGI) and make such amounts available to the Franchise Tax Board (FTB) in the form of a use tax table for calendar year 2012 and subsequent years.

PUBLIC HEARING

The Board will conduct a meeting in Room 121, at 450 N Street, Sacramento, California, on March 20-22, 2012. The Board will provide notice of the meeting to any person who requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board's Website at www.boe.ca.gov at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 9:30 a.m. or as soon thereafter as the matter may be heard on March 20, 21, or 22, 2012. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulation 1685.5.

AUTHORITY

RTC section 7051.

REFERENCE

RTC section 6452.1.

INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW

Prior Law

RTC section 6452.1, as enacted by Statutes 2010, chapter 721, section 2, permits taxpayers to make an irrevocable election to report “qualified use tax” on an “acceptable [income] tax return” filed with the FTB in order to make it more convenient for taxpayers to comply with their use tax obligations. RTC section 6452.1, subdivision (d)(2), as enacted by Statutes 2010, chapter 721 defined the term “qualified use tax” to mean a taxpayer’s actual unpaid use tax liability after applying the state use taxes imposed under the Sales and Use Tax Law (RTC § 6001 et seq.) and section 35 of article XIII of the California Constitution, and the local and district use taxes imposed in conformity with the Bradley-Burns Uniform Local Sales and Use Tax Law (RTC § 7200 et seq.) or in accordance with the Transactions and Use Tax Law (RTC § 7251 et seq.) to the taxpayer’s purchases of tangible personal property subject to use tax.

Current Law

SB 86 was enacted on March 23, 2011. It amended RTC section 6452.1 to make it more convenient for taxpayers to comply with their use tax obligations by giving taxpayers the option to report their “estimated use tax liabilities,” based upon their AGIs for income tax purposes, for one or more single nonbusiness purchases of individual items of tangible personal property each with a sales price of less than one thousand dollars (\$1000), as determined from a use tax table, instead of calculating and reporting their actual unpaid use tax liabilities (as described above). In addition, RTC section 6452.1, subdivision (d)(2)(A)(i)(II), as amended by SB 86, provides that “the Board shall annually calculate the estimated amount of use tax due according to a person’s adjusted gross income and by July 30 of each calendar year make available to [the] Franchise Tax Board such amounts in the form of a use tax table” for inclusion in the instructions to the FTB’s returns and use by eligible taxpayers.

Regulation 1685.5

The Board adopted Regulation 1685.5 on July 26, 2011, to prescribe the use tax table that taxpayers may use to estimate their calendar-year 2011 use taxes based upon their AGIs, prescribe the manner in which the Board shall annually calculate the estimated amount of use tax due according to a person’s AGI for calendar year 2012 and subsequent years, and prescribe the format of the use tax tables the Board must make available to the FTB each year. The California Taxpayers Association (CalTax) requested that the Board conduct interested parties meetings to discuss the methodology used to develop the proposed regulation before the Board voted to adopt Regulation 1685.5. The Board’s response to this request, as provided in the final statement of reasons for the adoption of Regulation 1685.5, was that:

“[T]he Board did not have adequate time to conduct interested parties meetings before initiating the formal rulemaking process to adopt proposed Regulation 1685.5 because:

- The use tax table provisions were added to RTC section 6452.1 on March 23, 2011;
- The Board needed to adopt a 2011 use tax table and forward it to the FTB for inclusion in the instructions to the FTB's 2011 income tax returns by the July 30, 2011, deadline specified in RTC section 6452.1; and
- The FTB needs to know that the 2011 use tax table adopted by the Board has been approved by OAL by September 1 and will be effective for use with 2011 income tax returns so that the FTB can include the 2011 use tax table in the instructions to its 2011 income tax returns, which will be sent out for publication and incorporation into return preparation software on September 1, 2011.

However, the Board has already scheduled interested parties meetings to discuss whether the Board needs to amend Regulation 1685.5 before the July 30, 2012, deadline, in which it is required to estimate consumers' 2012 use tax liabilities based upon their adjusted gross incomes and prepare a 2012 use tax table for transmission to the FTB."

Proposed Amendments

Board staff met with interested parties on August 29, 2011, and October 11, 2011, to discuss whether it is necessary to amend Regulation 1685.5 to update the manner in which the Board shall annually calculate the estimated amount of use tax due according to a person's AGI and make such amounts available to the FTB in the form of a use tax table for calendar year 2012 and subsequent years. As a result of public comments, including comments from CalTax, Board staff recommended that the Board amend Regulation 1685.5 to:

- Clarify that the Board's use tax tables are optional and may only be used to report estimated use tax for nonbusiness purchases of individual items of tangible personal property each with a sales price of less than \$1,000, as provided in RTC section 6452.1, subdivision (d)(2)(A)(i);
- Provide assurance to consumers that if they correctly report their estimated use tax liabilities for their eligible nonbusiness purchases in accordance with the Board's use tax tables, then the Board may not assess the difference, if any, between the estimated use tax liabilities reported in accordance with the Board's use tax tables and the consumers' actual use tax liabilities, as provided in RTC section 6452.1, subdivision (g);
- Add seven additional AGI ranges to the Board's use tax tables for calendar year 2012 and subsequent years and narrow the intervals between the AGI ranges in the Board's use tax tables so that estimated use tax liabilities increase or decrease by smaller amounts between AGI ranges;
- Move the use tax liability factor calculation date from May 1 to June 1 beginning in calendar year 2012 because the United States Census Bureau typically publishes its electronic shopping and mail order house spending data during May of each year;
- Require the Board to make adjustments to the amount of spending at electronic shopping and mail order houses to arrive at total spending on taxable purchases;

- Require the Board to calculate the percentage of income spent on taxable purchases, rather than the percentage of income spent on all electronic and mail order house purchases; and
- Require the Board to use the percentage of income spent on taxable purchases, rather than the percentage of income spent on all electronic and mail order house purchases, to calculate the use tax liability factors for calendar-year 2012 and subsequent years.

During its December 14, 2011, Business Taxes Committee meeting, the Board determined that staff's recommended amendments are reasonably necessary to update the manner in which the Board shall annually calculate the estimated amount of use tax due according to a person's AGI and make such amounts available to the FTB in the form of a use tax table for calendar year 2012 and subsequent years, and the Board voted to propose their adoption. The objectives of the proposed amendments are to clarify the purpose and use of the Board's use tax tables, help ensure that use taxes due on business purchases are not reported twice, help ensure that the Board uses the most current United States Census Bureau data possible to calculate the use tax liability factors for 2012 and subsequent years, improve the overall precision of the Board's estimated amount of use tax due according to a person's AGI range, and generally encourage consumers to use the Board use tax tables. The proposed amendments are anticipated to provide the following specific benefits:

- Clarify the purpose and use of the Board's use tax tables;
- Help ensure that use taxes due on business purchases are not reported twice;
- Help ensure that the Board uses the most current United States Census Bureau data possible to calculate the use tax liability factors for 2012 and subsequent years;
- Improve the overall precision of the Board's estimated amount of use tax due according to a person's AGI range; and
- Generally encourage consumers to use the Board use tax tables.

The Board has performed an evaluation of whether the proposed amendments to Regulation 1685.5 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Regulation 1685.5 is the only state regulation prescribing the manner in which the Board "shall annually calculate the estimated amount of use tax due according to a person's adjusted gross income and by July 30 of each calendar year make available to [the] Franchise Tax Board such amounts in the form of a use tax table," as required by RTC section 6452.1, as amended by section 1 of SB 86.

There are no comparable federal regulations or statutes to Regulation 1685.5.

Note Regarding Assembly Bill No. (AB) 155 and the Use Tax Liability Factor

The proposed amendments to Regulation 1685.5, subdivision (b)(2), will require that the Board multiply the percentage of income spent on taxable purchases during the preceding

year by 0.37, which represents the estimated percentage of California consumers' total purchases of tangible personal property for use in California from all out-of-state retailers that are made from out-of-state retailers that are not registered with the Board to collect use tax from their customers. AB 155 (Stats. 2011, ch. 313) expanded the use tax registration requirements so that they apply to some out-of-state retailers, including Internet retailers, that were previously not required to register with the Board to collect and remit use tax on their sales of tangible personal property to California customers. However, section 6 of AB 155 provides that the new registration requirements will not be operative until either September 15, 2012, or January 1, 2013, and the Board is currently unable to determine whether the new registration requirements will reduce the percentage of California consumers' total purchases of tangible personal property for use in California from all out-of-state retailers that are made from out-of-state retailers that are not registered with the Board to collect use tax from their customers during 2012 or in subsequent years, and, if so, the extent of such reduction. Therefore, the Board is not proposing to amend Regulation 1685.5 to account for the new registration requirements imposed by AB 155 at this time. However, the Board is continuing to monitor the implementation of AB 155 and considering whether to propose sufficiently related changes to the original text of the proposed amendments to Regulation 1685.5 to account for the enactment of AB 155 or other events that may change the percentage of taxable purchases that California consumers make from unregistered out-of-state retailers during 2012 or subsequent years.

NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS

The Board has determined that the adoption of the proposed amendments to Regulation 1685.5 will not impose a mandate on local agencies or school districts, including a mandate that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code.

NO COST OR SAVINGS TO STATE AGENCIES, LOCAL AGENCIES, AND SCHOOL DISTRICTS

The Board has determined that the adoption of the proposed amendments to Regulation 1685.5 will result in no direct or indirect cost or savings to any state agency, any cost to local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS

The adoption of the proposed amendments to Regulation 1685.5 will update the manner in which the Board shall annually calculate the estimated amount of use tax due according to a person's AGI and make such amounts available to the FTB in the form of a use tax table for calendar year 2012 and subsequent years. The proposed amendments

will not impose any new taxes or change any exemptions or exclusions. Furthermore, the proposed amendments expressly provide that taxpayers are not required to use the Board's use tax tables to estimate and report their use tax liabilities. Therefore, the Board has made an initial determination that the adoption of the proposed amendments to Regulation 1685.5 will not have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states.

The adoption of the proposed amendments to Regulation 1685.5 may affect small business.

NO COST IMPACTS TO PRIVATE PERSONS OR BUSINESSES

The Board is not aware of any cost impacts that a representative private person or business would necessarily incur in reasonable compliance with the proposed action.

RESULTS OF THE ECONOMIC IMPACT ANALYSIS REQUIRED BY GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b)

The Board has prepared the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1). The Board has determined that the adoption of the proposed amendments to Regulation 1685.5 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California. Furthermore, the Board has determined that the adoption of the proposed amendments to Regulation 1685.5 will not affect the health and welfare of California residents, worker safety, or the state's environment.

NO SIGNIFICANT EFFECT ON HOUSING COSTS

Adoption of the proposed amendments to Regulation 1685.5 will not have a significant effect on housing costs.

DETERMINATION REGARDING ALTERNATIVES

The Board must determine that no reasonable alternative considered by it or that has been otherwise identified and brought to its attention would be more effective in carrying out the purpose for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost-effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

CONTACT PERSONS

Questions regarding the substance of the proposed amendments should be directed to Bradley M. Heller, Tax Counsel IV, by telephone at (916) 323-3091, by e-mail at

Bradley.Heller@boe.ca.gov, or by mail at State Board of Equalization, Attn: Bradley M. Heller, MIC:82, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0082.

Written comments for the Board's consideration, notice of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed administrative action should be directed to Mr. Rick Bennion, Regulations Coordinator, by telephone at (916) 445-2130, by fax at (916) 324-3984, by e-mail at Richard.Bennion@boe.ca.gov, or by mail at State Board of Equalization, Attn: Rick Bennion, MIC:80, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0080.

WRITTEN COMMENT PERIOD

The written comment period ends at 9:30 a.m. on March 20, 2012, or as soon thereafter as the Board begins the public hearing regarding the proposed amendments to Regulation 1685.5 during the March 20-22, 2012, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to adopt the proposed amendments to Regulation 1685.5. The Board will only consider written comments received by that time.

AVAILABILITY OF INITIAL STATEMENT OF REASONS AND TEXT OF PROPOSED REGULATION

The Board has prepared an underscored and strikeout version of the text of Regulation 1685.5 illustrating the express terms of the proposed amendments and an initial statement of reasons for the adoption of the proposed amendments. These documents and all the information on which the proposed amendments are based, including the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1), are available to the public upon request. The rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed amendments and the Initial Statement of Reasons are also available on the Board's Website at www.boe.ca.gov.

SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8

The Board may adopt the proposed amendments to Regulation 1685.5 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will make the full text of the proposed amendments, with the change clearly indicated, available to the public for at least 15 days before adoption. The text of the resulting amendments will be mailed to those interested parties who commented on the original proposed amendments orally or in writing or who asked to be informed of

such changes. The text of the resulting amendments will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting amendments that are received prior to adoption.

AVAILABILITY OF FINAL STATEMENT OF REASONS

If the Board adopts the proposed amendments to Regulation 1685.5, the Board will prepare a Final Statement of Reasons, which will be made available for inspection at 450 N Street, Sacramento, California, and available on the Board's Website at www.boe.ca.gov.